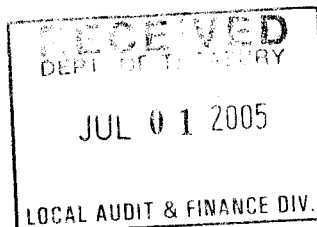


**FINANCIAL REPORT
CITY OF HARBOR SPRINGS
December 31, 2004**

Auditing Procedures Report

Issued under P.A. 2 of 1968, as amended.



Local Government Type <input checked="" type="checkbox"/> City <input type="checkbox"/> Township <input type="checkbox"/> Village <input type="checkbox"/> Other		Local Government Name City of Harbor Springs	County Emmet
Audit Date 12/31/04	Opinion Date 6/14/05	Date Accountant Report Submitted to State: 6/30/05	

We have audited the financial statements of this local unit of government and rendered an opinion on financial statements prepared in accordance with the Statements of the Governmental Accounting Standards Board (GASB) and the *Uniform Reporting Format for Financial Statements for Counties and Local Units of Government in Michigan* by the Michigan Department of Treasury.

We affirm that:

1. We have complied with the *Bulletin for the Audits of Local Units of Government in Michigan* as revised.
2. We are certified public accountants registered to practice in Michigan.

We further affirm the following. "Yes" responses have been disclosed in the financial statements, including the notes, or in the report of comments and recommendations

You must check the applicable box for each item below.

- ☐ Yes ☒ No 1. Certain component units/funds/agencies of the local unit are excluded from the financial statements.
- ☐ Yes ☒ No 2. There are accumulated deficits in one or more of this unit's unreserved fund balances/retained earnings (P.A. 275 of 1980).
- ☐ Yes ☒ No 3. There are instances of non-compliance with the Uniform Accounting and Budgeting Act (P.A. 2 of 1968, as amended).
- ☐ Yes ☒ No 4. The local unit has violated the conditions of either an order issued under the Municipal Finance Act or its requirements, or an order issued under the Emergency Municipal Loan Act.
- ☐ Yes ☒ No 5. The local unit holds deposits/investments which do not comply with statutory requirements. (P.A. 20 of 1943, as amended [MCL 129.91], or P.A. 55 of 1982, as amended [MCL 38.1132]).
- ☐ Yes ☒ No 6. The local unit has been delinquent in distributing tax revenues that were collected for another taxing unit.
- ☐ Yes ☒ No 7. The local unit has violated the Constitutional requirement (Article 9, Section 24) to fund current year earned pension benefits (normal costs) in the current year. If the plan is more than 100% funded and the overfunding credits are more than the normal cost requirement, no contributions are due (paid during the year).
- ☐ Yes ☒ No 8. The local unit uses credit cards and has not adopted an applicable policy as required by P.A. 266 of 1995 (MCL 129.241).
- ☐ Yes ☒ No 9. The local unit has not adopted an investment policy as required by P.A. 196 of 1997 (MCL 129.95).

We have enclosed the following:

	Enclosed	To Be Forwarded	Not Required
The letter of comments and recommendations.			✓
Reports on individual federal financial assistance programs (program audits).			✓
Single Audit Reports (ASLGU).			✓

Certified Public Accountant (Firm Name) Hill, Schroderus & Co., LLP			
Street Address 923 Spring Street		City Petoskey	State MI
Accountant Signature 		ZIP Code 49770	Date 6/30/05

**CITY OF HARBOR SPRINGS
FINANCIAL REPORT
December 31, 2004**

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Hill • Schroderus & Co., LLP
Certified Public Accountants & Consultants

June 14, 2005

Independent Auditors' Report

Honorable Mayor, Members of
City Council and City Manager
City of Harbor Springs, Michigan

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the discretely presented component unit, each major fund and the aggregate remaining fund information of the City of Harbor Springs, Michigan, as of and for the year ended December 31, 2004, which collectively comprise the City's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the City's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, the discretely presented component unit, each major fund and the aggregate remaining fund information of the City of Harbor Springs, as of December 31, 2004, and the respective changes in financial position and cash flows, where applicable, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The City has implemented a new financial reporting model, as required by the provisions of GASB Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*, as of January 1, 2004.

The management's discussion and analysis and budgetary comparison information, as listed in the table of contents, are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City of Harbor Springs' basic financial statements. The other supplemental information, as listed in the table of contents, is presented for purpose of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Hill, Schroeder & Co.

CERTIFIED PUBLIC ACCOUNTANTS
Petoskey, Michigan

City of Harbor Springs

160 Zoll Street * Post Office Box 678
Harbor Springs, Michigan 49740-0678
Phone: (231)526-2104 Fax: (231)526-6865

Frederick W. Geuder, City Manager
Ronald B. McRae, City Clerk/Comptroller/Treasurer
Dan Branson, Chief of Police

Alan Dika, Mayor
Jean Jardine, Mayor Pro-tem
Pringle Pfeifer, Council Member
Laura Kors, Council Member
Charles R. Baldwin, Council Member

MANAGEMENT'S DISCUSSION AND ANALYSIS

As management of the City of Harbor Springs, we offer readers of the City's financial statements this narrative overview and analysis of the financial activities of the City for the year ended December 31, 2004. The City has implemented a new financial reporting model, as required by the provisions of GASB Statement No. 34, Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments, as of January 1, 2004. Since 2004 is the initial year for this new financial reporting model, previous year comparisons will not be available until future years.

FINANCIAL HIGHLIGHTS:

Our financial status remained stable over the last year. Net assets for governmental activities total, \$5,642,198 at year-end which reflects an increase of \$184,260 from the previous year. Net assets for business type activities total, \$7,828,817 at year end which reflects a decrease of \$104,931 from the previous year.

Governmental activities expenses for the year were \$1,823,769. These activities generated \$172,999 in charges for services as well as \$270,831 in operating grants and contributions. Property taxes of \$1,127,371, transfers from business activities of \$242,149 and other general revenues of \$194,679 provided additional support for the governmental activities.

Business activities operating revenue for the year were \$4,295,685 and expenses \$4,228,888. Interest earnings and capital contributions provided additional revenue of \$70,421. Transfers to governmental activities of \$242,149 were made from net revenues and existing net assets.

OVERVIEW OF THE FINANCIAL STATEMENTS:

This discussion and analysis is intended to serve as an introduction to the City's basic financial statements. The City's basic financial statements are comprised of three components: 1) government wide financial statements, 2) fund financial statements and 3) notes to the financial statements. This report also contains other supplementary information in addition to the basic financial statements themselves.

GOVERNMENT-WIDE FINANCIAL STATEMENTS:

The government-wide financial statements are designed to provide readers with a broad overview of the City's finances in a manner similar to a private-sector business.

The Statement of Net Assets presents information on all of the City's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether financial position of the City is improving or deteriorating.

The Statement of Activities presents information showing how the City's net assets changed during the year. All changes in net assets are reported when the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in the future periods.

Both of the government-wide financial statements distinguish functions of the City that are principally supported by taxes and intergovernmental revenues (governmental activities) from functions that are intended to recover all or a significant portion of their costs through user fees and charges (business-type activities). The governmental activities of the City include general government and administration, public safety, public works and recreation and cultural. The business activities of the City include electric, water and sewer and waterfront operations.

FUND FINANCIAL STATEMENTS:

A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. All of the funds of the City can be divided into two categories – governmental funds and proprietary funds.

Governmental funds are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on current sources and uses of spendable resources, as well as on balances of spendable resources available at the end of the year. Such information may be useful in evaluating a government's near-term financing requirements.

The City maintains two types of proprietary funds. Enterprise funds are used to report the same functions as business-type activities in the government-wide financial statements. Internal service funds are an accounting device used to accumulate and allocate costs internally among the City's various functions. The City uses its internal service fund to account for motor vehicle and equipment usage. Because these services predominantly benefit governmental rather than business-type functions, they have been included within governmental activities in the government-wide financial statements.

FIDUCIARY FUNDS:

The City is a trustee or fiduciary for assets that are being held for the benefit of third parties. Since these funds cannot be used to address activities or obligations of the City, these funds do not appear in the government-wide financial statements.

NOTES TO THE FINANCIAL STATEMENTS:

The notes provide additional information which is essential to a full understanding of the data provided in the government-wide and fund financial statements.

GOVERNMENT-WIDE FINANCIAL ANALYSIS:

The table below summarizes the City's net assets as of December 31, 2004:

CITY OF HARBOR SPRINGS' NET ASSETS
December 31, 2004

	Governmental Activities	Business-Type Activities	Total
Assets			
Current and other assets	\$ 2,998,218	\$ 4,188,917	\$ 7,187,135
Capital assets-net of accum. dep.	4,387,131	4,150,569	8,537,700
Total assets	7,385,349	8,339,486	15,724,835
Liabilities			
Current	196,702	284,189	480,891
Noncurrent	1,546,449	226,480	1,772,929
Total liabilities	1,743,151	510,669	2,253,820
Net Assets			
Invested in capital assets, net of related debt	2,792,462	3,990,569	6,783,031
Restricted	49,682	27,500	77,182
Unrestricted	2,800,054	3,810,748	6,610,802
Total net assets	\$ 5,642,198	\$ 7,828,817	\$ 13,471,015

At the end of the year, the City of Harbor Springs is able to report positive balances in all three categories of net assets. The largest portion of the City's net assets is its investment in capital assets (land, buildings, equipment, improvements, construction in progress and infrastructure), less any related debt used to acquire those assets that is still outstanding.

The second portion of net assets, restricted net assets, represents resources that are subject to external restrictions on how they may be used. This would include restrictions for the SK-8 Park, Police Department and development fee payback.

The remaining portion of net assets, unrestricted net assets, may be used at the City's discretion to meet ongoing obligations.

The results for the City as a whole are reported in the Statement of Activities, which is summarized below:

CITY OF HARBOR SPRINGS' CHANGE IN NET ASSETS
Year Ended December 31, 2004

	Governmental Activities	Business-Type Activities	Total
Revenues			
Program revenues:			
Charges for services	\$ 172,999	\$ 4,295,685	\$ 4,468,684
Operating grants and contributions	270,831	-	270,831
Capital grants and contributions	-	17,001	17,001
General revenues:			
Property taxes	1,127,371	-	1,127,371
State-shared revenues	119,014	-	119,014
Interest and investment earnings	50,946	53,420	104,366
Miscellaneous	24,719	-	24,719
Total revenues	<u>1,765,880</u>	<u>4,366,106</u>	<u>6,131,986</u>
Expenses			
General government	169,725	-	169,725
Public safety	658,396	-	658,396
Public works	557,422	-	557,422
Recreation and cultural	204,722	-	204,722
Other	28,179	-	28,179
Interest on long-term debt	56,802	-	56,802
Unallocated depreciation	148,523	-	148,523
Electric	-	2,700,136	2,700,136
Water and sewer	-	1,102,644	1,102,644
Waterfront	-	426,108	426,108
Total expenses	<u>1,823,769</u>	<u>4,228,888</u>	<u>6,052,657</u>
Change in net assets before transfers	(57,889)	137,218	79,329
Transfers	<u>242,149</u>	<u>(242,149)</u>	<u>-</u>
Change in net assets	184,260	(104,931)	79,329
Net assets-beginning of year	<u>5,457,938</u>	<u>7,933,748</u>	<u>13,391,686</u>
Net assets-end of year	<u>\$ 5,642,198</u>	<u>\$ 7,828,817</u>	<u>\$ 13,471,015</u>

As reported above, the City incurred approximately \$1.8 million in governmental expenses. These expenses were funded primarily with property taxes (62%), operating grants and contributions (15%, mostly from the State for streets), transfers from the Electric and Water and Sewer Funds (13%) and charges for services (9%).

Business-type activities had an increase in net assets before transfers to governmental activities of \$137,218. Combined business-type and governmental activities net assets experienced less than a 1% increase during the year.

FUND FINANCIAL ANALYSIS:

At the end of the year, the governmental funds reported a combined fund balance of approximately \$2.4 million, which was \$83,726 higher than at the beginning of the year. The City did not undertake any large governmental capital projects during the year. The Zoll Street Building project for the city hall and police department was nearly complete at the beginning of the year. \$93,501 was expended on the project during the year.

The proprietary funds net assets remained stable at approximately \$7.8 million. The Electric Fund generated income before transfers of \$262,057 while the Water and Sewer Fund incurred a \$130,767 loss before transfers. The Waterfront Fund was essentially unchanged, incurring a \$11,073 loss. The Waterfront improvements to the West Dock of \$58,505 have been capitalized and will be depreciated over their estimated useful life.

General Fund budgetary highlights are that the actual results did not vary in any significant way from the budgetary plan. An unreserved ending fund balance of \$1,136,000 was budgeted. The ending unreserved fund balance actually was \$1,158,790. The schedule presented as required supplementary information indicates an actual ending fund balance of \$1,260,256, which includes amounts reserved for inventories, prepaids, SK-8 Park, and police department. Overall expenditures were less than budgeted. The transfer in from the Electric Fund was \$43,700 less than budgeted. The most significant change from the originally adopted budget to the final budget was to increase the parks and grounds budget by \$47,500 primarily for the land purchase adjacent to Kiwanis Park.

CAPITAL ASSET AND LONG TERM-DEBT ACTIVITY:

At the end of the year the capital assets, net of accumulated depreciation and long-term debt were:

Capital Assets

Governmental Activities: \$ 4,387,131
Business Type Activities: \$ 4,150,569

Long term Debt

Governmental Activities: \$1,546,449
Business Type Activities: \$226,480

Major capital activity during the year included completion of the Zoll Street Building project, acquisition of property adjacent to the Kiwanis Park and the start of work on the West Dock project.

Major debt activity during the year included advance refunding the 1994 Series Bonds to reduce future debt payments over the next six years by \$15,564.

KNOWN FACTORS AFFECTING FUTURE OPERATIONS:

The city plans to maintain its General Fund services at the same level, and does not anticipate any major changes to its cash or fund balances. No major General Fund capital expenditures are anticipated over the next five years. The City does intend to continue funding its street funding at the same levels over the next five years, and repair projects in the Major and Local Streets funds will vary by year, depending on the scope of projects completed. The fund balance in the streets funds will fluctuate accordingly.

The Waterfront Fund will fund improvements as needed. During the fiscal year ending December 31, 2005, the City will spend over \$200,000 including upgrades to the electric distribution system on the east floating dock, improvements to the two-hour "Shoppers' Dock", and the completion of renovations to the west dock. The renovations to the west dock include the removal and replacement of the decking material, removal of old pilings, and the addition of steel stringers for dock stability. These improvements are all funded by revenues and cash balances of the Waterfront Fund, and do not include any General Fund appropriations. Following completion of these projects in 2005, the City will review future capital needs and fund them as cash balances are replenished and increased with Waterfront revenues.

The Electric Fund continues to provide reliable electric service to both City and out-of-city customers with the City's Service Area. It is anticipated that the City will contract for a system-wide study of its facilities in 2006. One potential project that is anticipated is the construction of a second Sub-Station. The City will also continue to review potential capacity generation purchases, as they become available. The City has committed to the purchase of a share of the Michigan electric transmission grid, with the goal of stabilizing its transmission "wheeling" costs over the long term. As a member of the Michigan Public Power Agency, the City will look to the Agency for its long-term electric supply needs. All improvements and upgrades, as well as capacity and transmission services are funded by Electric Fund revenues.

The Water and Sewer Fund reviews its capital needs on an annual basis and budgets for improvements as necessary. When the City performs major street repairs, the City reviews whether it is prudent to make water or sewer repairs/improvements at the same time. By maintaining sufficient cash balances in the Water and Sewer Fund, the City can pay for the needed repairs and upgrades without General Fund contributions. The City does not anticipate any expansions to the service area over the next five years.

REQUEST FOR INFORMATION:

This financial report is designed to present users with a general overview of the City's finances and to demonstrate the entity's accountability for the revenues it receives. Questions concerning any of the information provided in this report or requests for additional financial information should be directed to the City Clerk's office, City of Harbor Springs.

CITY OF HARBOR SPRINGS
Statement of Net Assets
December 31, 2004

	Primary Government			Component Unit
	Governmental	Business-Type	Total	Downtown Development Authority
	Activities	Activities		Authority
<u>Assets</u>				
Current Assets				
Cash	\$ 2,598,476	\$ 2,873,468	\$ 5,471,944	\$ 524
Investments	74,028	-	74,028	-
Receivables:				
Accounts	1,016	690,155	691,171	-
Interest	11,011	12,241	23,252	-
Due from fiduciary fund	39,176	1,260	40,436	-
Due from component unit	524	-	524	-
Due from other governmental units	184,472	-	184,472	-
Inventories	14,851	327,389	342,240	-
Prepaid expenses	48,917	16,541	65,458	-
Total current assets	<u>2,972,471</u>	<u>3,921,054</u>	<u>6,893,525</u>	<u>524</u>
Noncurrent Assets				
Restricted assets:				
Customer deposits	-	106,480	106,480	-
Bond covenants	-	79,091	79,091	-
MPPA working capital advance	-	82,292	82,292	-
Deferred charges	25,747	-	25,747	-
Capital assets	9,172,361	8,180,153	17,352,514	-
Less: accumulated depreciation	<u>(4,785,230)</u>	<u>(4,029,584)</u>	<u>(8,814,814)</u>	<u>-</u>
Total noncurrent assets	<u>4,412,878</u>	<u>4,418,432</u>	<u>8,831,310</u>	<u>-</u>
Total assets	<u>\$ 7,385,349</u>	<u>\$ 8,339,486</u>	<u>\$ 15,724,835</u>	<u>\$ 524</u>
<u>Liabilities and Net Assets</u>				
Current Liabilities				
Accounts payable	\$ 19,979	\$ 171,709	\$ 191,688	\$ -
Accrued expenses	33,584	31,395	64,979	-
Due to primary government	-	-	-	524
Due to other governmental units	26,242	41,085	67,327	-
Accrued interest	9,328	-	9,328	-
Payable from restricted assets:				
Current portion of bonds payable	-	40,000	40,000	-
Bonds payable, due within one year	<u>107,569</u>	<u>-</u>	<u>107,569</u>	<u>-</u>
Total current liabilities	<u>196,702</u>	<u>284,189</u>	<u>480,891</u>	<u>524</u>
Noncurrent Liabilities				
Payable from restricted assets:				
Customer deposits	-	106,480	106,480	-
Compensated absences payable	33,602	-	33,602	-
Bonds payable, net	<u>1,512,847</u>	<u>120,000</u>	<u>1,632,847</u>	<u>-</u>
Total noncurrent liabilities	<u>1,546,449</u>	<u>226,480</u>	<u>1,772,929</u>	<u>-</u>
Total liabilities	<u>1,743,151</u>	<u>510,669</u>	<u>2,253,820</u>	<u>524</u>
Net Assets				
Invested in capital assets, net of related debt	2,792,462	3,990,569	6,783,031	-
Restricted for:				
SK-8 Park	14,272	-	14,272	-
Police department	35,410	-	35,410	-
Development fee payback	-	27,500	27,500	-
Unrestricted	<u>2,800,054</u>	<u>3,810,748</u>	<u>6,610,802</u>	<u>-</u>
Total net assets	<u>5,642,198</u>	<u>7,828,817</u>	<u>13,471,015</u>	<u>-</u>
Total liabilities and net assets	<u>\$ 7,385,349</u>	<u>\$ 8,339,486</u>	<u>\$ 15,724,835</u>	<u>\$ 524</u>

See accompanying notes to the basic financial statements. 3

CITY OF HARBOR SPRINGS
Statement of Activities
For the Year Ended December 31, 2004

Functions/Programs	Expenses	Program Revenues			Net (Expense) Revenue and Changes in Net Assets			Component Unit Downtown Development Authority
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Primary Government			
					Governmental Activities	Business-Type Activities	Total	
Primary Government								
Governmental activities:								
General government	\$ 169,725	\$ 18,444	\$ 24,818	\$ -	\$ (126,463)	\$ -	\$ (126,463)	\$ -
Public safety	658,396	122,755	12,185	-	(523,456)	-	(523,456)	-
Public works	557,422	-	217,724	-	(339,698)	-	(339,698)	-
Recreation and cultural	204,722	31,800	16,104	-	(156,818)	-	(156,818)	-
Other	28,179	-	-	-	(28,179)	-	(28,179)	-
Interest on long-term debt	56,802	-	-	-	(56,802)	-	(56,802)	-
Unallocated depreciation	148,523	-	-	-	(148,523)	-	(148,523)	-
Total governmental activities	1,823,769	172,999	270,831	-	(1,379,939)	-	(1,379,939)	-
Business-type activities:								
Electric	2,700,136	2,939,073	-	17,001	-	255,938	255,938	-
Water and sewer	1,102,644	953,369	-	-	-	(149,275)	(149,275)	-
Waterfront	426,108	403,243	-	-	-	(22,865)	(22,865)	-
Total business-type activities	4,228,888	4,295,685	-	17,001	-	83,798	83,798	-
Total primary government	\$ 6,052,657	\$ 4,468,684	\$ 270,831	\$ 17,001	(1,379,939)	83,798	(1,296,141)	-
Component Unit								
Downtown Development Authority	\$ 524	\$ -	\$ -	\$ -	-	-	-	(524)
General revenues:								
Property taxes					1,127,371	-	1,127,371	-
State-shared revenues					119,014	-	119,014	-
Interest and investment earnings					50,946	53,420	104,366	3
Miscellaneous					24,719	-	24,719	-
Transfers					242,149	(242,149)	-	-
Total general revenues and transfers					1,564,199	(188,729)	1,375,470	3
Change in net assets					184,260	(104,931)	79,329	(521)
Net assets - beginning of year					5,457,938	7,933,748	13,391,686	521
Net assets - end of year					\$ 5,642,198	\$ 7,828,817	\$ 13,471,015	\$ -

See accompanying notes to the basic financial statements.

CITY OF HARBOR SPRINGS
Balance Sheet
Governmental Funds
December 31, 2004

<u>Assets</u>	<u>General</u>	<u>Major Street</u>	<u>Local Street</u>	<u>Other Nonmajor Governmental Funds</u>	<u>Total Governmental Funds</u>
Cash	\$ 1,070,475	\$ 118,741	\$ 798,430	\$ 129,529	\$ 2,117,175
Investments	-	-	-	74,028	74,028
Receivables:					
Accounts	-	-	-	825	825
Accrued interest	4,853	485	2,901	576	8,815
Due from other funds	39,700	-	-	-	39,700
Due from other governmental units	152,378	25,416	6,678	-	184,472
Inventories	6,671	-	-	8,180	14,851
Prepaid expenditures	45,113	221	137	245	45,716
	<u>\$ 1,319,190</u>	<u>\$ 144,863</u>	<u>\$ 808,146</u>	<u>\$ 213,383</u>	<u>\$ 2,485,582</u>
Total assets					
	<u>\$ 1,319,190</u>	<u>\$ 144,863</u>	<u>\$ 808,146</u>	<u>\$ 213,383</u>	<u>\$ 2,485,582</u>
<u>Liabilities and Fund Balances</u>					
Liabilities					
Accounts payable	\$ 10,598	\$ -	\$ -	\$ 1,875	\$ 12,473
Accrued expenditures	22,094	1,297	199	221	23,811
Due to other governmental units	26,242	-	-	-	26,242
	<u>58,934</u>	<u>1,297</u>	<u>199</u>	<u>2,096</u>	<u>62,526</u>
Total liabilities					
	<u>58,934</u>	<u>1,297</u>	<u>199</u>	<u>2,096</u>	<u>62,526</u>
Fund balances					
Reserved for:					
Inventories and prepaids	51,784	221	137	8,425	60,567
SK-8 Park	14,272	-	-	-	14,272
Police department	35,410	-	-	-	35,410
Unreserved:					
Undesignated	1,158,790	143,345	807,810	202,862	2,312,807
	<u>1,260,256</u>	<u>143,566</u>	<u>807,947</u>	<u>211,287</u>	<u>2,423,056</u>
Total fund balances					
	<u>1,260,256</u>	<u>143,566</u>	<u>807,947</u>	<u>211,287</u>	<u>2,423,056</u>
Total liabilities and fund balances					
	<u>\$ 1,319,190</u>	<u>\$ 144,863</u>	<u>\$ 808,146</u>	<u>\$ 213,383</u>	<u>\$ 2,485,582</u>

CITY OF HARBOR SPRINGS
Reconciliation of Governmental Funds Balance Sheet to the
Statement of Net Assets
December 31, 2004

Total Fund Balance - Governmental Funds	\$ 2,423,056
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Amounts reported for governmental activities in the statement of net assets are different because:

Governmental funds report capital outlays as expenditures. However, in the statement of net assets, these assets are capitalized and depreciated over their estimated useful lives. Includes capital assets of Internal Service Fund.

Governmental capital assets	9,172,361
Accumulated depreciation	(4,785,230)

Governmental funds report interest when due, whereas in the statement of net assets, interest is accrued on outstanding bonds. (9,328)

Long-term liabilities, including bonds payable, are not due and payable in the current period and therefore are not reported in the governmental funds. Includes Internal Service Fund.

Governmental bonds payable	(1,620,416)
Compensated absences	(33,602)

Internal service funds are used to charge costs of certain activities, such as motor vehicle usage, to various departments within the City. The assets and liabilities of the Internal Service Fund are included in government activities in the statement of net assets.

Internal Service Fund balances not included in other reconciling items:

Current assets	486,889
Deferred charges	25,747
Accounts payable and accrued expenses	<u>(17,279)</u>

Net Assets of Governmental Activities	\$ <u>5,642,198</u>
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CITY OF HARBOR SPRINGS
Statement of Revenues, Expenditures, and Changes in Fund Balances
Governmental Funds
For the Year Ended December 31, 2004

	General	Major Street	Local Street	Other Nonmajor Governmental Funds	Total Governmental Funds
Revenues					
Taxes	\$ 1,127,371	\$ -	\$ -	\$ -	\$ 1,127,371
Licenses and permits	15,480	-	-	-	15,480
State grants	119,014	168,801	48,923	-	336,738
Charges for services	152,610	-	-	1,965	154,575
Fines and forfeits	2,944	-	-	-	2,944
Interest and investment earnings	19,634	1,988	11,811	10,823	44,256
Other	44,341	-	-	22,088	66,429
Total revenues	1,481,394	170,789	60,734	34,876	1,747,793
Expenditures					
Current:					
General government	234,386	-	-	-	234,386
Public safety	656,948	-	-	1,448	658,396
Public works	271,743	139,762	145,917	-	557,422
Recreation and cultural	235,462	-	-	22,171	257,633
Other	28,179	-	-	-	28,179
Capital outlay	-	-	-	93,501	93,501
Total expenditures	1,426,718	139,762	145,917	117,120	1,829,517
Excess (deficiency) of revenues over expenditures	54,676	31,027	(85,183)	(82,244)	(81,724)
Other financing sources (uses)					
Operating transfers in	165,000	-	113,300	27,100	305,400
Operating transfers out	(140,400)	-	-	-	(140,400)
Total other financing sources (uses)	24,600	-	113,300	27,100	165,000
Net change in fund balances	79,276	31,027	28,117	(55,144)	83,276
Fund balances - beginning of year	1,180,980	112,539	779,830	266,431	2,339,780
Fund balances - end of year	\$ 1,260,256	\$ 143,566	\$ 807,947	\$ 211,287	\$ 2,423,056

CITY OF HARBOR SPRINGS
Reconciliation of the Statement of Revenues, Expenditures, and
Changes in Fund Balances of Governmental Funds to the
Statement of Activities
For the Year Ended December 31, 2004

Net Change in Fund Balances - Total Governmental Funds \$ 83,276

Amounts reported for governmental activities in the statement of activities
are different because:

Governmental funds report capital outlays as expenditures. However,
in the statement of activities, the cost of these assets is allocated over
their estimated useful lives as depreciation.

Expenditures for capital assets	146,412
Current year depreciation	(148,523)

Repayment of bond principal is an expenditure in the governmental
funds, but the repayment reduces long-term liabilities in the statement
of net assets. This is the amount of principal paid on long-term debt. 25,000

Interest on long-term debt is recognized as an expenditure when it is
due in the governmental funds. However, in the statement of activities,
interest expense is recognized as the interest accrues, regardless of
when it is due. 167

Compensated absences are recognized as an expenditure when it is paid
in the governmental funds. In the statement of activities, however,
compensated absences are recognized as an expense when earned. (17,308)

Internal service funds are used to charge costs of certain activities,
such as insurance and motor vehicle usage, to various departments
within the City. The net revenue (expense) of the internal service funds
are included in governmental activities in the statement of activities. 95,236

Change in Net Assets of Governmental Activities \$ 184,260

CITY OF HARBOR SPRINGS
Statement of Net Assets
Proprietary Funds
December 31, 2004

	Business-Type Activities - Enterprise Funds				Governmental Activities - Internal Service Fund
	Electric System	Water and Sewer System	Waterfront	Totals Current Year	
<u>Assets</u>					
Current Assets					
Cash	\$ 1,209,444	\$ 1,174,510	\$ 489,514	\$ 2,873,468	\$ 481,301
Receivables:					
Accounts	571,975	117,980	200	690,155	191
Accrued interest	5,338	4,430	2,473	12,241	2,196
Due from other funds	-	1,260	-	1,260	-
Inventories	279,089	48,300	-	327,389	-
Prepaid expenses	10,178	5,377	986	16,541	3,201
Total current assets	<u>2,076,024</u>	<u>1,351,857</u>	<u>493,173</u>	<u>3,921,054</u>	<u>486,889</u>
Noncurrent Assets					
Restricted assets:					
Customer deposits	62,330	15,350	28,800	106,480	-
Bond covenants	-	-	79,091	79,091	-
MPPA working capital advance	82,292	-	-	82,292	-
Deferred charges	-	-	-	-	25,747
Capital assets	4,099,009	2,235,643	1,845,501	8,180,153	2,589,090
Less: accumulated depreciation	<u>(2,013,361)</u>	<u>(1,172,820)</u>	<u>(843,403)</u>	<u>(4,029,584)</u>	<u>(1,239,209)</u>
Total noncurrent assets	<u>2,230,270</u>	<u>1,078,173</u>	<u>1,109,989</u>	<u>4,418,432</u>	<u>1,375,628</u>
Total assets	<u>\$ 4,306,294</u>	<u>\$ 2,430,030</u>	<u>\$ 1,603,162</u>	<u>\$ 8,339,486</u>	<u>\$ 1,862,517</u>

CITY OF HARBOR SPRINGS
Statement of Net Assets
Proprietary Funds
(Continued)
December 31, 2004

	<u>Business-Type Activities - Enterprise Funds</u>				<u>Governmental Activities - Internal Service Fund</u>
	<u>Electric System</u>	<u>Water and Sewer System</u>	<u>Waterfront</u>	<u>Totals Current Year</u>	
<u>Liabilities and Net Assets</u>					
Current Liabilities					
Accounts payable	\$ 149,911	\$ 2,649	\$ 19,149	\$ 171,709	\$ 7,506
Accrued expenses	14,826	15,209	1,360	31,395	9,773
Due to other governmental units	-	34,801	6,284	41,085	-
Bonds payable due within one year	-	-	-	-	82,569
Total current liabilities	<u>164,737</u>	<u>52,659</u>	<u>26,793</u>	<u>244,189</u>	<u>99,848</u>
Current Liabilities (payable from restricted assets)					
Current portion of bonds payable	<u>-</u>	<u>-</u>	<u>40,000</u>	<u>40,000</u>	<u>-</u>
Noncurrent Liabilities					
Payable from restricted assets:					
Customer deposits	62,330	15,350	28,800	106,480	-
Bonds payable (net of current portion, unamortized premiums, issuance costs, and deferred amount on refunding)	<u>-</u>	<u>-</u>	<u>120,000</u>	<u>120,000</u>	<u>462,847</u>
Total noncurrent liabilities	<u>62,330</u>	<u>15,350</u>	<u>148,800</u>	<u>226,480</u>	<u>462,847</u>
Total liabilities	<u>227,067</u>	<u>68,009</u>	<u>215,593</u>	<u>510,669</u>	<u>562,695</u>
Net Assets					
Invested in capital assets, net of related debt	2,085,648	1,062,823	842,098	3,990,569	-
Restricted for development fee payback	27,500	-	-	27,500	-
Unrestricted	<u>1,966,079</u>	<u>1,299,198</u>	<u>545,471</u>	<u>3,810,748</u>	<u>1,299,822</u>
Total net assets	<u>4,079,227</u>	<u>2,362,021</u>	<u>1,387,569</u>	<u>7,828,817</u>	<u>1,299,822</u>
Total liabilities and net assets	<u>\$ 4,306,294</u>	<u>\$ 2,430,030</u>	<u>\$ 1,603,162</u>	<u>\$ 8,339,486</u>	<u>\$ 1,862,517</u>

CITY OF HARBOR SPRINGS
Statement of Revenues, Expenses, and Changes in Fund Net Assets
Proprietary Funds
For the Year Ended December 31, 2004

	Business-Type Activities - Enterprise Funds				Governmental Activities - Internal Service Fund
	Electric System	Water and Sewer System	Waterfront	Totals Current Year	
Operating revenues					
Charges for services	\$ 2,871,069	\$ 940,736	\$ 403,243	\$ 4,215,048	\$ 361,486
Operating expenses					
Purchased power	1,562,498	-	-	1,562,498	-
Personal services	386,500	208,934	99,386	694,820	29,436
Contractual services	384,516	719,429	212,817	1,316,762	93,731
Other supplies and expenses	201,583	95,679	20,023	317,285	57,517
Heat, light and power	24,739	20,789	15,708	61,236	5,318
Depreciation	140,300	57,813	64,194	262,307	139,030
Amortization	-	-	-	-	-
Total operating expenses	2,700,136	1,102,644	412,128	4,214,908	325,032
Operating income (loss)	170,933	(161,908)	(8,885)	140	36,454
Nonoperating revenues					
Interest	23,120	18,508	11,792	53,420	6,690
Development fees	68,004	12,633	-	80,637	-
Miscellaneous	-	-	-	-	9,813
Total nonoperating revenues	91,124	31,141	11,792	134,057	16,503
Nonoperating expenses					
Interest	-	-	13,980	13,980	34,870
Total nonoperating revenues (expenses)	91,124	31,141	(2,188)	120,077	(18,367)
Income (loss) before operating transfers and capital contributions	262,057	(130,767)	(11,073)	120,217	18,087
Other financing sources (uses)					
Operating transfers in	-	-	-	-	77,149
Operating transfers out	(220,106)	(22,043)	-	(242,149)	-
Total other financing sources (uses)	(220,106)	(22,043)	-	(242,149)	77,149
Capital contributions	17,001	-	-	17,001	-
Change in net assets	58,952	(152,810)	(11,073)	(104,931)	95,236
Total net assets - beginning	4,020,275	2,514,831	1,398,642	7,933,748	1,204,586
Total net assets - ending	\$ 4,079,227	\$ 2,362,021	\$ 1,387,569	\$ 7,828,817	\$ 1,299,822

CITY OF HARBOR SPRINGS
Statement of Cash Flows
Proprietary Funds
For the Year Ended December 31, 2004

	Business-Type Activities - Enterprise Funds				Governmental Activities - Internal Service Fund
	Electric System	Water and Sewer System	Waterfront	Totals Current Year	
Cash flows from operating activities					
Receipts from customers	\$ 2,795,913	\$ 934,256	\$ 403,043	\$ 4,133,212	\$ 361,486
Payments to suppliers	(2,204,199)	(826,555)	(247,236)	(3,277,990)	(153,935)
Payments to employees	(377,494)	(213,521)	(99,055)	(690,070)	(29,258)
Net cash provided (used) by operating activities	214,220	(105,820)	56,752	165,152	178,293
Cash flows from non-capital financing activities					
Operating transfers-in from other funds	-	-	-	-	77,149
Operating transfers-out to other funds	(220,106)	(22,043)	-	(242,149)	-
Net cash provided (used) by non-capital financing activities	(220,106)	(22,043)	-	(242,149)	77,149
Cash flows from capital and related financing activities					
Acquisition and construction of capital assets and contracts payable	(8,448)	(44,036)	(41,532)	(94,016)	(64,051)
Principal paid on bonds	-	-	(40,000)	(40,000)	(75,000)
Interest paid on bonds	-	-	(13,980)	(13,980)	(35,212)
Development fees	68,004	12,633	-	80,637	-
Capital contributed by customers	17,001	-	-	17,001	-
Net cash provided by miscellaneous non-operating activities	-	-	-	-	9,813
MPPA working capital advance	(82,292)	-	-	(82,292)	-
Net cash provided (used) for capital and related financing activities	(5,735)	(31,403)	(95,512)	(132,650)	(164,450)
Cash flows from investing activities					
Interest received	17,910	14,203	9,381	41,494	5,037
Net cash provided (used) from investing activities	17,910	14,203	9,381	41,494	5,037
Net increase (decrease) in cash	6,289	(145,063)	(29,379)	(168,153)	96,029
Cash, beginning	1,265,485	1,334,923	626,784	3,227,192	385,272
Cash, ending	<u>\$ 1,271,774</u>	<u>\$ 1,189,860</u>	<u>\$ 597,405</u>	<u>\$ 3,059,039</u>	<u>\$ 481,301</u>
Classified as:					
Current assets	\$ 1,209,444	\$ 1,174,510	\$ 489,514	\$ 2,873,468	\$ 481,301
Restricted assets	62,330	15,350	107,891	185,571	-
Totals	<u>\$ 1,271,774</u>	<u>\$ 1,189,860</u>	<u>\$ 597,405</u>	<u>\$ 3,059,039</u>	<u>\$ 481,301</u>

CITY OF HARBOR SPRINGS
Statement of Cash Flows
Proprietary Funds
(Continued)
For the Year Ended December 31, 2004

	<u>Business-Type Activities - Enterprise Funds</u>				<u>Governmental Activities - Internal Service Fund</u>
	<u>Electric System</u>	<u>Water and Sewer System</u>	<u>Waterfront</u>	<u>Totals Current Year</u>	
Reconciliation of operating income to net cash provided (used) by operating activities					
Operating income (loss)	\$ 170,933	\$ (161,908)	\$ (8,885)	\$ 140	\$ 36,454
Adjustments to reconcile operating income to net cash provided by operating activities:					
Depreciation	140,300	57,813	64,194	262,307	139,030
(Increase) decrease in accounts receivable	(81,968)	(6,830)	(200)	(88,998)	-
(Increase) decrease in inventory	(40,229)	(8,233)	-	(48,462)	-
(Increase) decrease in due from other funds	-	-	-	-	-
(Increase) decrease in prepaid expenses	(574)	(233)	1,956	1,149	419
Increase (decrease) in accounts payable	9,940	1,725	(6,928)	4,737	2,212
Increase (decrease) in accrued expenses	9,006	(4,587)	331	4,750	178
Increase (decrease) in due to other funds	-	-	-	-	-
Increase (decrease) in due to other governmental units	-	16,083	6,284	22,367	-
Increase (decrease) in deposits	6,812	350	-	7,162	-
Total adjustments	43,287	56,088	65,637	165,012	141,839
Net cash provided (used) by operating activities	<u>\$ 214,220</u>	<u>\$ (105,820)</u>	<u>\$ 56,752</u>	<u>\$ 165,152</u>	<u>\$ 178,293</u>

CITY OF HARBOR SPRINGS
Statement of Fiduciary Net Assets
Fiduciary Funds
December 31, 2004

	<u>Agency Funds</u>
<u>Assets</u>	
Cash	\$ 363,207
Receivables:	
Taxes	2,582,120
Water sales	<u>2,593</u>
Total assets	<u>\$ 2,947,920</u>
<u>Liabilities</u>	
Due to other funds	\$ 40,436
Due to other governmental units	3,220
Due to County	827,129
Due to School	1,112,458
Due to State	51,720
Due to ISD	423,005
Due to College	361,488
Due to Medical Care Facility	75,468
Due to Cemetery	26,336
Due to Ambulance and EMS	23,235
Other liabilities	<u>3,425</u>
Total liabilities	<u>\$ 2,947,920</u>

See accompanying notes to the basic financial statements.

**CITY OF HARBOR SPRINGS
NOTES TO FINANCIAL STATEMENTS
December 31, 2004**

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The City of Harbor Springs (the City) was incorporated October 6, 1932, under the provisions of Act 279, P.A. 1909, as amended (Home Rule City Act). The City operates under a Council-Manager form of government and provides the following services as authorized by its charter: public safety (police and fire), highways and streets, sanitation, health and social services, culture-recreation, public improvements, planning and zoning, and general administrative services.

The City's financial statements are prepared in accordance with generally accepted accounting principles (GAAP). The Governmental Accounting Standards Board (GASB) is the standard-setting body for governmental accounting and financial reporting. The City's reporting entity applies all relevant Governmental Accounting Standards Board (GASB) pronouncements. Proprietary funds and similar component units apply Financial Accounting Standards Board (FASB) pronouncements and Accounting Principles Board (APB) opinions issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements, in which case, GASB prevails. Pronouncements of the FASB issued after November 30, 1989 are not applied in the preparation of the financial statements of the proprietary funds and similar component units in accordance with GASB Statement No. 20. The following is a summary of the significant policies used by the City of Harbor Springs:

REPORTING ENTITY

These financial statements present the City (the primary government) and its component unit. As defined by GASBS No. 14, component units are legally separate entities that are included in the City's reporting entity because of the significance of their operating or financial relationships with the City. The primary government is required to consider other organizations for which the nature and significance of their relationship with the primary government are such that exclusion would cause the reporting entity's financial statements to be misleading or incomplete.

Discretely Presented Component Unit

Downtown Development Authority – The Downtown Development Authority, which was established pursuant to the provisions of Public Act 197 of 1975, as amended, is governed by a nine-member board appointed by the City Council. The Authority may issue debt subject to limitations set forth in the Act, but may not expend any monies without prior approval of City Council. Separate financial statements for the Downtown Development Authority are not issued.

NOTES TO FINANCIAL STATEMENTS – CONTINUED

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

BASIC FINANCIAL STATEMENTS – OVERVIEW

The City of Harbor Spring's basic financial statements include both government-wide (reporting the City as a whole) and fund financial statements (reporting the City's major funds). Both the government-wide and the fund financial statements categorize primary government activities as either governmental or business type. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business type activities, which rely to a significant extent on fees and charges for support. The primary government is reported separately from legally separate component units for which the primary government is financially accountable.

BASIC FINANCIAL STATEMENTS – GOVERNMENT-WIDE STATEMENTS

The government-wide financial statements report information on all of the nonfiduciary activities of the primary government and its component units. As a general rule the effect of interfund activity, such as overhead costs, has been eliminated from these statements. The government-wide focus is more on operational efficiency, the sustainability of the City as an entity and the change in the City's net assets resulting from the current year's activities.

Internal service funds are consolidated into the governmental column when presented at the government-wide level. This is because the principal users of the internal service are the City's governmental activities. The net profit/loss in the internal service funds is allocated to the functional activity (public safety, public works, etc.) based upon usage.

In the government-wide Statement of Net Assets, both the governmental and business type activities are presented on a consolidated basis. Due to the full accrual, economic resource basis, all long-term assets and receivables, as well as long-term debt and obligations are recognized. The City's net assets are reported in three parts – invested in capital assets, net of related debt; restricted net assets; and unrestricted net assets. The City first utilizes restricted resources to finance qualifying activities.

The government-wide Statement of Activities demonstrates the degree to which the direct expenses of a given function or segment are offset by program revenues. This statement reduces gross expenses (including depreciation) by related program revenues, which include charges for services, operating grants and capital grants.

The program revenues must be directly associated with the function or segment. Program revenues include: (1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment; and (2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or segment. Taxes and other items not properly included among program revenues are reported as general revenue.

NOTES TO FINANCIAL STATEMENTS-CONTINUED

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

BASIC FINANCIAL STATEMENTS – FUND FINANCIAL STATEMENTS

The financial transactions of the City are reported in individual funds in the fund financial statements. Each fund is accounted for by providing a separate set of self-balancing accounts that comprise its assets, liabilities, fund balances, revenues and expenditures/expenses. The focus of the fund financial statements is upon the determination of financial position and changes in financial position (sources, uses, and balances of financial resources).

Government resources are allocated to and accounted for in individual funds based upon the purposes for which they are to be spent and the means by which spending activities are controlled. The emphasis in the fund financial statements is on the major funds in the governmental or business type categories. GASBS No. 34 sets forth minimum criteria (percentage of the assets, liabilities, revenues or expenditures/expenses of the governmental and proprietary funds) for the determination of major funds.

Governmental Funds

The following is a description of the major governmental funds of the City:

General Fund – The General Fund is the general operating fund of the City. It is used to account for all financial resources except those required to be accounted for in another fund.

Major and Local Street Funds – The Street Funds account for the operation of the street departments. Primary financing is provided by the City's share of state gasoline taxes. State law requires these gasoline taxes be used to maintain streets.

In addition, the City reports the following non-major governmental funds:

Special Revenue Funds

Police Reserve Fund – The City performs record keeping functions for this fund while the City Council approves all transactions. Primary financing is through contributions.

Historical Commission Fund – The City performs record keeping functions for this fund while the City Council approves all transactions. Primary financing is through contributions.

Capital Project Fund

Capital Project Fund – The Capital Project Fund is being used to account for the Zoll Street Buildings project to remodel, improve, construct, furnish and equip two existing buildings to serve as a city hall and police department facility.

NOTES TO FINANCIAL STATEMENTS – CONTINUED

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

BASIC FINANCIAL STATEMENTS – FUND FINANCIAL STATEMENTS – CONTINUED

Proprietary Funds

The focus of the proprietary funds is upon the determination of operating income, changes in fund net assets, financial position, and cash flows, which is similar to for-profit businesses. The following is a description of the major proprietary funds of the City:

Electric Fund – The Electric Fund is an Enterprise Fund. The fund is financed and operated in a manner similar to a private enterprise. The intent is that costs (expenses, including depreciation) of providing electricity to the general public are recovered through user charges.

Water and Sewer Fund – The Water and Sewer Fund is an Enterprise Fund. The fund is financed and operated in a manner similar to a private enterprise. The intent is that costs (expenses, including depreciation) of providing water and sewer services to the general public are recovered through user charges.

Waterfront Fund – The Waterfront Fund is an Enterprise Fund. The fund is financed and operated in a manner similar to a private enterprise. The intent is that costs (expenses, including depreciation) of providing City boat docking and mooring services to the general public are recovered through user charges.

In addition, the City reports the following non-major proprietary funds:

Motor Vehicle and Equipment Fund – The Motor Vehicle and Equipment Fund is an internal service fund. This fund accounts for the cost of acquiring, maintaining and providing vehicle and equipment usage to various City departments.

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operation. The principal operating revenues of the Electric, Water and Sewer, Waterfront, and Motor Vehicle and Equipment Funds are charges to customers for sales and services. Operating expenses for these funds include the cost of sales and services, administrative expenses and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

Fiduciary Funds

The fiduciary funds are used to account for assets held by the City in a trustee or agent capacity. Since, by definition, these assets are being held for the benefit of a third party (other local governments, private parties, pension participants, etc.) and cannot be used to address activities or obligations of the government, these funds are not incorporated into the government-wide statements.

NOTES TO FINANCIAL STATEMENTS – CONTINUED

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

BASIC FINANCIAL STATEMENTS – FUND FINANCIAL STATEMENTS – CONTINUED

Agency funds use the accrual basis of accounting, however report only assets and liabilities.

Agency Fund – The Agency Fund accounts for the collection and payment of property tax levies, payroll withholdings, nonprofit organization receipts and water billings.

BASIS OF ACCOUNTING

Basis of accounting refers to the point at which revenues and expenditures/expenses are recognized in the accounts and reported in the financial statements. Basis of accounting relates to the timing of the measurements made, regardless of the measurement focus applied.

The government-wide statements are reported using the economic resources measurement focus and the full accrual basis of accounting, which incorporates long-term assets and receivables as well as long-term debt and obligations. Revenue is recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenue in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met. Expenditures generally are recorded when a liability is incurred.

All proprietary funds, pension trust funds and agency funds are accounted for using the full accrual basis of accounting. Their revenues are recognized when they are earned and their expenses are recognized when they are incurred. Unbilled Water and Sewer and Electric Fund utility service receivables are recorded at year-end.

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recorded in the accounting period in which they are earned, as long as they are both available and measurable. Revenues are available when received within the current period or within 60 days after year end. Expenditures are recorded in the accounting period in which the liability is incurred, as under full accrual accounting. However, debt service expenditures, expenditures relating to compensated absences, and claims and judgments are recorded only when payment is due.

ASSETS, LIABILITIES, AND NET ASSETS OR EQUITY

Cash and Cash Equivalents

Cash and cash equivalents are considered to be cash on hand and demand deposits.

Inventory

Inventory is valued at cost, which approximates market, using the first-in, first-out method. Inventory in the Historical Commission Fund consists of books and essays, which are recorded as expenditures when sold rather than when purchased.

NOTES TO FINANCIAL STATEMENTS – CONTINUED

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

ASSETS, LIABILITIES, AND NET ASSETS OR EQUITY – CONTINUED

Interfund Receivables/Payables

Outstanding balances between funds are reported as "due to/from other funds" on the balance sheet of the fund financial statements and as "internal balances" on the Statement of Net Assets of the government-wide financial statements.

Capital Assets

Capital assets, which include property, buildings, equipment and infrastructure assets (e.g., roads, bridges, sidewalks and similar items) are reported in the applicable governmental or business type activities column in the government-wide financial statements. Capital assets are recorded by the City when the initial individual costs are equal to or greater than the following amounts:

<u>Asset Type</u>	<u>Amount</u>
Land	\$ 1
Equipment	3,000
Buildings & Building improvements	10,000
Infrastructure	10,000

Capital assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation.

Property, buildings and equipment are depreciated using the straight-line method over the following useful lives:

Buildings	40 to 60 years
Building Improvements	20 to 60 years
Water and Sewer Lines	50 to 75 years
Streets, Curbs and Gutters	10 to 30 years
Electric Lines and Appurtenances	30 to 50 years
Vehicles (Pickup Trucks & Automobiles)	3 to 7 years
Vehicles (Large Trucks and Fire Trucks)	10 to 25 years
Office Equipment	5 to 7 years
Office Furniture	5 to 15 years

Long-Term Obligations

In the government-wide financial statements and the proprietary fund financial statements, long-term debt and other long-term obligations are reported as liabilities. Bond premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bonds.

In the fund financial statements, governmental fund types recognize bond premiums and discounts, as well as bond issuance costs during the current period. The face amount of debt issued is reported as other financing sources. Premiums received on debt issuances are reported as other financing sources while discounts are reported as other financing uses.

NOTES TO FINANCIAL STATEMENTS – CONTINUED

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

ASSETS, LIABILITIES, AND NET ASSETS OR EQUITY – CONTINUED

Compensated Absences (Vacation and Sick Time)

Vacation days not used during the year may not be accumulated. Due to contract years differing from the City's fiscal year, unpaid vacation time represents unused, but not accumulated, vacation time. Sick time not used during the year may be accumulated. Upon retirement or death of an employee, he/she or his/her beneficiary is eligible to receive accumulated sick leave pay, up to a maximum dollar amount.

All vacation, sick pay, and other employee benefit amounts accrue when earned in the government-wide and proprietary fund financial statements. Sick and vacation pay are recognized in the governmental financial statements when the time is used.

Fund Equity

In the fund financial statements, governmental funds report reservations of fund balance for amounts that are not available for appropriation or are legally restricted by outside parties for a specific purpose. Designations of fund balance represent tentative management plans that are subject to change.

COMPARATIVE DATA

Comparative data for the prior year is not included in the City's financial statements.

ACCOUNTING CHANGE

In June 1999, the Governmental Accounting Standards Board (GASB) unanimously approved Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*. Effective January 1, 2004, the City implemented the provisions of GASB No. 34. Changes to the City's financial statements as a result of GASB No. 34 are as follows:

- A Management's Discussion and Analysis (MD&A) section providing analysis of the City's overall financial position and results of operations.
- Government-wide financial statements (Statement of Net Assets and Statement of Activities) prepared using full accrual accounting for all of the City's activities.
- A change in the fund financial statements with a focus on major funds.
- Capital assets in the governmental activities column of the Statement of Net Assets include assets which were previously reported in the General Fixed Asset Account Group.
- Liabilities in the governmental column of the Statement of Net Assets include bonds and other long-term obligations which were previously reported in the General Long-Term Debt Account Group.

NOTES TO FINANCIAL STATEMENTS – CONTINUED

NOTE 2: STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

Annual budgets are adopted on a basis consistent with generally accepted accounting principles for all operating funds of the City except for the agency funds. Budgetary control is legally maintained at the fund level.

The City follows these procedures in establishing the budgetary data reflected in the financial statements:

1. Prior to December 1, the City Manager submits to the City Council a proposed operating budget for the fiscal year commencing the following January 1. The operating budget includes proposed expenditures/expenses and the means of financing them.
2. A public hearing is conducted at City Hall to obtain taxpayer comments.
3. Prior to January 1, the fund budgets are legally enacted through passage of resolutions.
4. The City Manager is authorized to transfer budgeted amounts between departments within any fund; however, any revisions that alter the total expenditures/expenses of any fund must be approved by the City Council.
5. Formal budgetary integration is employed as a management control device during the year for the General and Special Revenue Funds.
6. Budgeted amounts are as originally adopted, or as amended by the City Council.
7. All appropriations lapse at year-end.

The General Fund Budgetary information includes administrative charges by the General Fund to various other funds as revenue of the General Fund. They have been offset against General Fund expenditures in the preparation of the basic financial statements. These charges remain as administrative expenditures/expenses of the various funds charged in the basic financial statements.

The City did not have an excess of expenditures over appropriations for the General Fund or its Special Revenue Funds.

NOTE 3: CASH AND INVESTMENTS

Michigan Compiled Laws, Section 129.91, authorizes the City to make deposits and invest in the accounts of federally insured banks, credit unions, and savings and loan associations which have an office in Michigan. The City is allowed to invest in bonds, securities and other direct obligations of the United States or any agency or instrumentality of the United States; United States government or federal agency obligations; repurchase agreements; bankers' acceptance of United States banks; commercial paper rated within the two highest classifications which mature not more than 270 days after the date of purchase; obligations of the State of Michigan or its political subdivisions which are rated as investment grade; and mutual funds composed of investment vehicles which are legal for direct investment by local units of government in Michigan.

The City's deposits and investment policy are in accordance with statutory authority.

NOTES TO FINANCIAL STATEMENTS – CONTINUED

NOTE 3: CASH AND INVESTMENTS –CONTINUED

Cash Deposits

At December 31, 2004, the carrying amount of the City's deposits was \$ 6,020,516 and the bank balance was \$ 6,524,292.

Pooling of Cash - The City pools cash to maximize its investment return.

<u>Fund</u>	<u>Amount</u>
Primary Government	
General	\$ 1,068,855
Major Street	118,741
Local Street	798,430
Electric System	1,271,774
Water and Sewer System	1,189,860
Waterfront	597,405
Other Nonmajor Governmental Funds	129,429
Internal Service Fund	<u>481,301</u>
Total	5,655,795
Fiduciary Funds	<u>1,887</u>
Total pooled cash	5,657,682
Cash not held in pooled accounts:	
Primary government	1,720
Component Unit	524
Fiduciary Funds	<u>361,320</u>
Total cash	<u><u>\$ 6,021,246</u></u>
Unrestricted cash (primary government)	\$ 5,471,944
Unrestricted cash (component unit)	524
Unrestricted cash (fiduciary funds)	363,207
Restricted cash (primary government)	<u>185,571</u>
Total cash	<u><u>\$ 6,021,246</u></u>

NOTES TO FINANCIAL STATEMENTS – CONTINUED

NOTE 3: CASH AND INVESTMENTS - CONTINUED

Federal Depository Insurance

Of the above balance in cash, \$600,000 was covered by federal depository insurance. The remaining amount was uninsured and uncollateralized. The City may experience significant fluctuations in deposit balances through the year.

Restricted Assets

Restricted assets consist of cash restricted in the Waterfront Fund in accordance with revenue bond indentures. Total restricted assets at December 31, 2004 were \$185,571.

Investments

Investments are stated at market value. Investments held at a financial institution can be categorized according to three levels of risk. The three levels of risk are:

Category 1	Investments that are insured, registered or held by the entity or by its agent in the City's name.
Category 2	Investments that are uninsured and unregistered held by the counterparty's trust department or agent in the City's name.
Category 3	Uninsured and unregistered investments held by the counterparty, its trust or its agent, but not in the City's name.

The City has stock with a market value of \$74,028 at December 31, 2004. This investment is classified by risk level as Category 1.

The City of Harbor Springs has mutual fund investments with the ICMA Retirement Corporation. The nature of the mutual funds does not allow for risk categorization, which is in accordance with GASB Statement No. 3 for the defined contribution plan.

NOTE 4: PROPERTY TAXES

Property taxes are levied and become a lien on property as of July 1 on the State taxable valuation of property in the City as of the preceding December 31. The City bills and collects its own property taxes and also collects taxes for other governmental units. Collection of other governmental unit's taxes and remittance of them to the units are accounted for in the Agency Fund. Property taxes are recognized as revenue in the year for which they are levied.

The City is permitted by charter to levy taxes, subject to State Headlee and Truth in Taxation provisions, up to \$15 per \$1,000 of taxable valuation for general governmental services and for the payment of principal and interest on general obligation long-term debt. The 2004 State taxable valuation of the City of Harbor Springs totaled \$177,509,071.

The tax rate for the year ended December 31, 2004, was as follows:

<u>Purpose</u>	<u>Rate/Taxable Valuation</u>
General governmental services	5.9592 per \$1,000

NOTES TO FINANCIAL STATEMENTS – CONTINUED

NOTE 5: INTERFUND RECEIVABLES AND PAYABLES

The interfund balances within the primary government are as follows:

	Interfund Receivable	Interfund Payable
General Fund	\$ 39,176	\$ -
Water and Sewer Fund	1,260	-
Fiduciary Funds	-	40,436
	<u>\$ 40,436</u>	<u>\$ 40,436</u>

The interfund balances between the primary government and the component units are as follows:

	Interfund Receivable	Interfund Payable
General Fund	\$ 524	\$ -
D.D.A.	-	524
	<u>\$ 524</u>	<u>\$ 524</u>

The interfund balances are mainly for property taxes.

NOTE 6: INTERFUND TRANSFERS

Operating transfers within the primary government are as follows:

	Transfer In	Transfer Out
General Fund	\$ 165,000	\$ 140,400
Local Street Fund	113,300	-
Electric Fund	-	220,106
Water and Sewer Fund	-	22,043
Other Nonmajor Govt. Funds	27,100	-
Internal Service Funds	77,149	-
	<u>\$ 382,549</u>	<u>\$ 382,549</u>

There were no operating transfers between the primary government and the component unit during the year.

The operating transfers are mainly for street improvements, debt service, equipment purchases, and general City operations.

NOTES TO FINANCIAL STATEMENTS – CONTINUED

NOTE 7: CAPITAL ASSETS

Capital asset activity of the City's primary government for the current year was as follows:

	Balance January 1, 2004	Additions	Deletions	Balance December 31, 2004
Governmental Activities				
Capital assets not being depreciated:				
Land	\$ 870,165	\$ 45,725	\$ -	\$ 915,890
Capital assets being depreciated:				
Buildings and improvements	1,375,126	1,917,080	-	3,292,206
Street, curbs, sidewalks and storm sewers	3,435,294	-	-	3,435,294
Office equipment	17,596	-	-	17,596
Furniture & equipment	90,769	89,467	(4,370)	175,866
Machinery & equipment	1,339,511	49,199	(53,201)	1,335,509
Construction in progress	1,861,464	-	(1,861,464)	-
Subtotal	8,119,760	2,055,746	(1,919,035)	8,256,471
Less Accumulated Depreciation:				
Building and improvements	(225,359)	(31,730)	-	(257,089)
Street, curbs, sidewalks, and storm sewers	(3,435,294)	-	-	(3,435,294)
Office equipment	(17,596)	-	-	(17,596)
Furniture & equipment	(39,503)	(16,474)	4,370	(51,607)
Machinery & equipment	(976,526)	(100,319)	53,201	(1,023,644)
Construction in progress	-	-	-	-
Subtotal	(4,694,278)	(148,523)	57,571	(4,785,230)
Net capital assets being depreciated	3,425,482	1,907,223	(1,861,464)	3,471,241
Governmental activities net capital assets	\$ 4,295,647	\$ 1,952,948	\$ (1,861,464)	\$ 4,387,131

NOTES TO FINANCIAL STATEMENTS – CONTINUED

NOTE 7: CAPITAL ASSETS – CONTINUED

	Balance January 1, 2004	Additions	Deletions	Balance December 31, 2004
Business-type Activities				
Capital assets not being depreciated:				
Land	\$ 314,913	\$ -	\$ -	\$ 314,913
Capital assets being depreciated:				
Buildings and improvements	1,511,421	44,036	-	1,555,457
Equipment	6,242,829	8,449	-	6,251,278
Construction in progress	-	58,505	-	58,505
Subtotal	<u>7,754,250</u>	<u>110,990</u>	<u>-</u>	<u>7,865,240</u>
Less accumulated depreciation:				
Buildings and improvements	(797,862)	(62,102)	-	(859,964)
Equipment	(2,969,415)	(200,205)	-	(3,169,620)
Construction in progress	-	-	-	-
Subtotal	<u>(3,767,277)</u>	<u>(262,307)</u>	<u>-</u>	<u>(4,029,584)</u>
Net capital assets being depreciated	<u>3,986,973</u>	<u>(151,317)</u>	<u>-</u>	<u>3,835,656</u>
Business-type activities net capital assets	<u>\$ 4,301,886</u>	<u>\$ (151,317)</u>	<u>\$ -</u>	<u>\$ 4,150,569</u>

NOTES TO FINANCIAL STATEMENTS – CONTINUED

NOTE 7: CAPITAL ASSETS – CONTINUED

Depreciation expense was charged to the primary government as follows:

Governmental Activities

Unallocated	\$ 9,493
Internal service fund capital assets consolidated with the governmental activities	<u>139,030</u>
Total governmental activities	<u>\$ 148,523</u>

Business-type Activities

Electric	140,300
Water and sewer	57,813
Waterfront	<u>64,194</u>
Total business-type activities	<u>\$ 262,307</u>

Construction Commitments

The City has active construction projects at year-end. The projects include:

	<u>Project Estimates</u>	<u>Expended to Dec. 31, 2004</u>	<u>Committed</u>
West dock improvements	<u>\$ 125,000</u>	<u>\$ 58,505</u>	<u>\$ 66,495</u>

At year-end, all construction in progress amounts are capitalized.

Proprietary Fund Type Property, Plant and Equipment

Proprietary fund type property, plant and equipment at December 31, 2004 are summarized as follows:

	<u>Enterprise</u>	<u>Internal Service</u>
Land	\$ 314,913	\$ 36,640.00
Buildings and improvements	1,555,457	1,156,545
Equipment	6,251,278	1,395,905
Construction in progress	<u>58,505</u>	<u>-</u>
Total	8,180,153	2,589,090
Less: accumulated dep.	<u>(4,029,584)</u>	<u>(1,239,209)</u>
Net	<u>\$ 4,150,569</u>	<u>\$ 1,349,881</u>

NOTES TO FINANCIAL STATEMENTS – CONTINUED

NOTE 8: DEFERRED CHARGES

Debt issuance cost within the Motor Vehicle and Equipment Fund of \$25,747 relating to the 2004 General Obligation Bonds are being amortized as interest expense using the straight-line method over the 6-year life of the 2004 bonds. Interest expense of \$0 was recognized in the current year; unamortized amounts at year-end amounted to \$25,747.

NOTE 9: LEASE OBLIGATIONS

The City has entered into lease agreements with the Harbor Springs Area Fire Authority for fire protection services. The City uses the land, building, and equipment to provide fire protection services to the constituent municipalities making up the Harbor Springs Area Fire Authority.

The current lease agreements with the Authority call for annual lease payments from the Authority to the City of \$50 for the land and building lease, and annual payments from the City to the Authority of \$5 for the sublease of land and buildings, and \$5 for the lease of fire protection equipment.

The City has a lease agreement with the State of Michigan Department of Natural Resources ('DNR') for a parcel of Lake Michigan bottomland where the City's West Doc is located. The original lease terms call for annual payments to the DNR through 2014. Lease rates are adjusted in years ending in "0" or "5". The terms allow for one renewal of 25 years at the City's option. The lease amount for the year ending December 31, 2004 was \$4,387.

The City also has a lease agreement with the State of Michigan Department of Environmental Quality for the mooring fields. The lease fees are 10% of annual mooring revenues. For the year ended December 31, 2004, the lease fees were \$5,704.

NOTE 10: DEFERRED COMPENSATION PLAN

The City offers its employees a deferred compensation plan created in accordance with Internal Revenue Code 457. The plan, available to all City employees, permits them to defer a portion of their salary until future years. The deferred compensation is not available to employees until termination, retirement, death, or unforeseeable emergency.

All amounts of compensation deferred under the plan, all property and rights purchased with those amounts, and all income attributable to those amounts, property, or rights were (until paid or made available to the employee or other beneficiary) solely the property and rights of the City (without being restricted to the provisions of benefits under the plan), subject only to the claims of the City's general creditors. Participants' rights under the plan were equal to those of general creditors of the City in an amount equal to the fair market value of the deferred account for each participant.

In complying with the amended Section 457 requirements, these assets are now for the exclusive benefit of participants and not subject to the claims of the City's general creditors. As such, they are no longer included in an agency fund of the City.

The City made contributions to this deferred compensation plan based on 8% to 12% of gross salary for the year. The total deferred compensation plan contributions for 2004 were \$55,531.

Employer contributions subsequent to year-end were transferred to the Michigan Municipal Employees Retirement System (MERS) an agent multiple employer defined pension plan. Employee contributions remain in this plan. No new contributions are being accepted, the plan is "dormant".

NOTES TO FINANCIAL STATEMENTS – CONTINUED

NOTE 11: **DEFINED CONTRIBUTION PLAN**

The City provided pension benefits for its full-time union employees through a defined contribution plan. In a defined contribution plan, benefits depend solely on amounts contributed to the plan plus investment earnings. Employees are eligible to participate upon employment. Union agreements required the City to contribute 7% to 8% of each employee's base wages to their individual accounts. Employees could also contribute to their individual accounts. Employer contributions and earnings of each individual employee fully vested after seven years of credited service. Contributions and earnings not vested with employees who left employment were used to offset the cost of succeeding employer contributions.

The City's total plan payroll in fiscal year 2004 was \$742,793. The City made the required contribution, amount to \$57,540. Volunteer employee contributions amounted to \$654.

Employer contributions, subsequent to year-end, were also transferred to the MERS plan. Some employee contributions were also voluntarily transferred to the new plan. The City will no longer make contributions to the defined contribution plan. Voluntary employee contributions to the defined contribution plan are still being accepted.

NOTE 12: **OTHER POST-EMPLOYEE BENEFITS**

The City provides post-employment benefits of health insurance to eligible employees. The City funds these benefits on a pay-as-you-go basis as necessary. For the year ended December 31, 2004, there were seven participants. The City's expense was approximately \$79,435.

NOTES TO FINANCIAL STATEMENTS – CONTINUED

NOTE 13: LONG-TERM DEBT

The following is a summary of the City's long-term debt transactions for the year ended December 31, 2004:

	Beginning Balance	Additions	Reductions	Ending Balance	Amount Due Within One Year
PRIMARY GOVERNMENT					
Governmental Activities					
Bonds and notes payable:					
General obligation debt					
1994 Series	\$ 600,000	\$ -	\$ 600,000	\$ -	\$ -
2002 Series	1,100,000	-	25,000	1,075,000	25,000
2004 Series	-	560,000	-	560,000	85,000
	1,700,000	560,000	625,000	1,635,000	110,000
Plus premium on bonds payable	-	5,215	-	5,215	869
Less deferred amount on refundings	-	(19,799)	-	(19,799)	(3,300)
Total bonds and notes payable	1,700,000	545,416	625,000	1,620,416	107,569
Other liabilities:					
Compensated absences	16,294	17,308	-	33,602	-
Total governmental activities long-term liabilities	<u>\$ 1,716,294</u>	<u>\$ 562,724</u>	<u>\$ 625,000</u>	<u>\$ 1,654,018</u>	<u>\$ 107,569</u>
Business Type Activities					
Bonds and notes payable:					
Revenue bonds					
1989 Marina improvement	<u>\$ 200,000</u>	<u>\$ -</u>	<u>\$ 40,000</u>	<u>\$ 160,000</u>	<u>\$ 40,000</u>

Long-term liabilities payable at December 31, 2004 is composed of the following individual issues:

\$1,125,000, 2002 Harbor Springs Building Authority General Obligation bonds due in annual installments of \$25,000 to \$75,000 through October 1, 2022; interest at 4.00% to 6.00%.	\$1,075,000
\$560,000, 2004 Harbor Springs General Obligation bonds due in annual installments of \$80,000 to \$105,000 through October 1, 2010; interest at 3.00% to 3.50%, net of premium and deferred amount on refundings.	545,416
Total governmental activities general obligation debt	1,620,416
Compensated Absences	33,602
Total governmental activities long-term liabilities	<u>\$1,654,018</u>

NOTES TO FINANCIAL STATEMENTS – CONTINUED

NOTE 13: LONG-TERM DEBT – CONTINUED

Business-Type Activities:

\$450,000, 1989 Marina Improvement Revenue Bonds due in annual installments of \$40,000 through September 1, 2008; interest at 6.95% to 7.00%.

\$160,000

The annual debt service requirements to maturity for all general and revenue obligation bonds outstanding excluding premium and refunding deferrals, as of December 31, 2004, are as follows:

Year Ending December 31	Governmental Activities		Business-Type Activities	
	Principal	Interest	Principal	Interest
2005	\$ 110,000	\$ 69,579	\$ 40,000	\$ 11,200
2006	110,000	69,980	40,000	8,400
2007	130,000	66,430	40,000	5,600
2008	155,000	61,030	40,000	2,800
2009	155,000	54,878	-	-
2010 - 2014	375,000	200,215	-	-
2015 - 2019	375,000	114,746	-	-
2020 - 2024	225,000	23,062	-	-
2025 - 2029	-	-	-	-
Total	<u>\$ 1,635,000</u>	<u>\$ 659,920</u>	<u>\$ 160,000</u>	<u>\$ 28,000</u>

Advance Refunding

On December 22, 2004, the City issued \$560,000 in General Obligation Bonds with an average Interest rate of 3.22%. The proceeds of these bonds were used to advance refund \$525,000 of outstanding 1994 Series bonds with an average interest rate of 5.75%. The net proceeds of \$539,467 (after payment of \$25,747 in underwriting fees and other issuance costs) were used to purchase U. S. government securities. Those securities were deposited in an irrevocable trust with an escrow agent to provide for all future debt service payments on the 1994 Series bonds. As a result, the 1994 Series bonds are considered to be defeased and the liability for those bonds has been removed from the government-wide statement of net assets.

The advance refunding resulted in a difference between the reacquisition price and the net carrying amount of the old debt of \$19,799. This difference, reported in the accompanying financial statements as a deduction from bonds payable, will be charged to interest expense on a straight-line basis over the original life of the 1994 Series bonds. The City completed the advance refunding to reduce its total debt service payments over the next 6 years by \$15,564 and to obtain an economic gain (difference between the present values of the old and new debt service payments) of \$14,910.

An original issue premium of \$5,215 is being amortized using the straight-line method over the life of the 2004 bonds. \$0 was recognized in the current year; unamortized amounts at year-end amounted to \$5,215.

NOTES TO FINANCIAL STATEMENTS – CONTINUED

NOTE 14: COMMITMENTS

Insurance Commitments

The City self-insures its workmen's compensation and unemployment compensation liabilities through their participation in workmen's compensation and unemployment compensation self-insurance groups.

Entitlement Commitments

- A. During 1979 and 1982, the Michigan Public Power Agency (MPPA), of which the City is a member, acquired an ownership interest in the Consumers Power Company Campbell No. 3 plant, related transmission lines and coal stockpile, and rights to back-up capacity and energy supplies from other Consumer generating units and resources.

The City's entitlement share of the Campbell No. 3 generating capacity is 500 (KW) which specifies minimum annual payments on a "take-or-pay" basis for the generation and transmission capability of the unit, through the year 2012.

- B. During 2001, the MPPA, of which the City is a member, acquired an ownership interest in the CT Project No. 1.

The City's entitlement share of the CT Project No. 1 generating capacity is 1,999(KW) which specifies minimum annual payments on a "take-or-pay" basis for the generation and transmission capability of the unit, through the year 2026.

- C. The City also has a take-or-pay contract with the Harbor Springs Area Sewage Disposal Authority for the construction of a sewer system. The control and ownership of the sewer facilities rests with the Authority.

The original 1989 Bonds were refunded in 2004. The faith and credit of the City has been pledged to pay its 63.84% share of the \$370,000 refunding bonds issued by the Harbor Springs Area Sewage Disposal Authority through the year 2009.

- D. In March 2002, the City entered into a contract with the Harbor Springs Area Sewage Disposal Authority for the City's share of the cost of a new wastewater treatment facility and the closure of the Authority's existing lagoon and spray irrigation system.

The faith and credit of the City has been pledged to pay its 39.28% share of the \$5,664,770 of bonds issued by the Harbor Springs Area Sewage Disposal Authority through the year 2023.

NOTES TO FINANCIAL STATEMENTS – CONTINUED

NOTE 14: COMMITMENTS – CONTINUED

Entitlement Commitments – Continued

The entitlements specify minimum annual payments as follows:

	Campbell No. 3 (A.)	CT Project No. 1(B.)	H. S. Sewage Authority (C.)	H.S. Sewage Authroity (D.)	Total
2005	\$ 48,838	\$ 109,688	\$ 51,780	\$ 140,746	\$ 351,052
2006	48,916	109,697	51,172	140,375	350,160
2007	48,951	109,811	52,967	141,995	353,724
2008	48,939	109,703	51,471	141,578	351,691
2009	39,901	109,732	52,987	141,111	343,731
2010 - 2014	120,605	548,954	-	706,243	1,375,802
2015 - 2019	-	548,776	-	706,292	1,255,068
2020 - 2024	-	548,916	-	563,447	1,112,363
2025 - 2029	-	219,543	-	-	219,543
Total payments	<u>\$ 356,150</u>	<u>\$ 2,414,820</u>	<u>\$ 260,377</u>	<u>\$ 2,681,787</u>	<u>\$ 5,713,134</u>

NOTE 15: CONTINGENCIES

The General Fund is contingently liable for the Waterfront, revenue obligation. The General Fund is obligated only if revenues of the fund would be insufficient to meet its debt service requirements.

The City is currently testing its landfill as a possible source of drinking water contamination. However, studies to date have been inconclusive. Thus, no provision has been made for any potential liability related to the landfill.

NOTE 16: RISK MANAGEMENT

The City is exposed to various risks of loss related to torts, theft of, damage to and destruction of assets; errors and omissions; injuries to employees and natural disasters. The City belongs to the Michigan Municipal League Liability and Property Pool, a public entity risk pool currently operating as a common risk management and insurance program for various municipalities throughout the state. The City pays an annual premium for its general insurance coverage. The pool is self-sustaining through member premiums and reinsures through commercial companies for claims in excess of \$500,000 for each insured event. Although the City could be assessed charges beyond the annual premium, the likelihood of receiving such an assessment is minimal. Settled claims have not exceeded coverage in any of the past three years.

REQUIRED SUPPLEMENTARY INFORMATION

CITY OF HARBOR SPRINGS
Budgetary Comparison Schedule
General Fund
For the Year Ended December 31, 2004

	Budgeted Amounts		Actual Amounts	Variance with Final Budget Over/(Under)
	Original	Final		
Beginning budgetary fund balance	<u>\$ 1,135,000</u>	<u>\$ 1,102,300</u>	<u>\$ 1,180,980</u>	<u>\$ 78,680</u>
Resources (inflows):				
Taxes	1,153,400	1,129,100	1,127,371	(1,729)
Licenses and permits	17,400	14,900	15,480	580
State grants	125,100	125,400	119,014	(6,386)
Administrative fees	386,700	386,700	386,668	(32)
Charges for services	165,200	137,600	152,610	15,010
Fines and forfeits	3,200	2,400	2,944	544
Interest	25,800	30,000	19,634	(10,366)
Other	37,500	37,000	44,341	7,341
Transfers from other funds	171,600	208,700	165,000	(43,700)
	<u>2,085,900</u>	<u>2,071,800</u>	<u>2,033,062</u>	<u>(38,738)</u>
Amounts available for appropriations				
Charges to appropriations (outflows):				
General government:				
Legislative	3,400	3,200	2,343	(857)
Manager	105,600	105,300	104,357	(943)
Elections	11,800	13,900	10,777	(3,123)
Accounting	137,500	131,800	125,502	(6,298)
Assessing	53,400	52,300	49,752	(2,548)
Legal services	74,000	53,000	50,369	(2,631)
Clerk	89,100	86,000	84,844	(1,156)
Finance treasurer	51,000	48,700	40,837	(7,863)
City hall and grounds	119,800	127,700	123,373	(4,327)
	<u>645,600</u>	<u>621,900</u>	<u>592,154</u>	<u>(29,746)</u>
Total general government				
Public safety:				
Police	499,300	486,200	471,135	(15,065)
Marine patrol	28,900	29,000	18,348	(10,652)
Fire	160,100	158,100	150,231	(7,869)
Planning	45,700	45,200	46,134	934
	<u>734,000</u>	<u>718,500</u>	<u>685,848</u>	<u>(32,652)</u>
Total public safety				
Public works:				
Cost of labor - sales	1,400	1,100	168	(932)
Spring clean-up	34,800	19,700	14,348	(5,352)
Leaf pickup	36,000	39,700	45,639	5,939
Sidewalks	45,700	50,700	49,407	(1,293)
Parking lots	15,300	19,300	22,536	3,236
Administration & fringe benefits	155,400	143,600	134,320	(9,280)
Airport activities	4,500	5,400	5,325	(75)
	<u>293,100</u>	<u>279,500</u>	<u>271,743</u>	<u>(7,757)</u>
Total public works				

CITY OF HARBOR SPRINGS
Budgetary Comparison Schedule
General Fund
(Continued)
For the Year Ended December 31, 2004

	<u>Budgeted Amounts</u>		<u>Actual Amounts</u>	<u>Variance with Final Budget Over/(Under)</u>
	<u>Original</u>	<u>Final</u>		
Recreation and cultural:				
SK-8 park	30,700	32,700	28,937	(3,763)
Beach	35,600	35,600	35,088	(512)
Kiwanis park	5,300	4,400	3,414	(986)
Ice rink	23,700	34,500	32,968	(1,532)
Parks and grounds	75,700	123,200	117,129	(6,071)
Deer park	7,100	5,000	2,513	(2,487)
Tree planting	24,100	11,300	8,797	(2,503)
Community promotion	8,700	7,400	6,616	(784)
Total recreation and cultural	<u>210,900</u>	<u>254,100</u>	<u>235,462</u>	<u>(18,638)</u>
Other functions	<u>24,500</u>	<u>23,700</u>	<u>28,179</u>	<u>4,479</u>
Transfers (out)	<u>185,100</u>	<u>140,400</u>	<u>140,400</u>	<u>-</u>
Total charges to appropriations	<u>2,093,200</u>	<u>2,038,100</u>	<u>1,953,786</u>	<u>(84,314)</u>
Ending budgetary fund balance	<u><u>\$ 1,127,700</u></u>	<u><u>\$ 1,136,000</u></u>	<u><u>\$ 1,260,256</u></u>	<u><u>\$ 124,256</u></u>

CITY OF HARBOR SPRINGS
Budgetary Comparison Schedule
Major Street Fund
For the Year Ended December 31, 2004

	<u>Budgeted Amounts</u>		<u>Actual Amounts</u>	<u>Variance with Final Budget Over/(Under)</u>
	<u>Original</u>	<u>Final</u>		
Beginning budgetary fund balance	<u>\$ 91,300</u>	<u>\$ 112,500</u>	<u>\$ 112,539</u>	<u>\$ 39</u>
Resources (inflows):				
State grants	123,800	152,000	168,801	16,801
Interest	<u>1,300</u>	<u>2,000</u>	<u>1,988</u>	<u>(12)</u>
Amounts available for appropriations	<u>125,100</u>	<u>154,000</u>	<u>170,789</u>	<u>16,789</u>
Charges to appropriations (outflows):				
Public works:				
Construction	-	-	-	-
Routine maintenance	76,200	87,700	77,362	(10,338)
Winter maintenance	34,600	37,100	42,903	5,803
Administration	8,000	8,000	8,000	-
Other	<u>21,000</u>	<u>21,500</u>	<u>11,497</u>	<u>(10,003)</u>
Total charges to appropriations	<u>139,800</u>	<u>154,300</u>	<u>139,762</u>	<u>(14,538)</u>
Ending budgetary fund balance	<u>\$ 76,600</u>	<u>\$ 112,200</u>	<u>\$ 143,566</u>	<u>\$ 31,366</u>

CITY OF HARBOR SPRINGS
Budgetary Comparison Schedule
Local Street Fund
For the Year Ended December 31, 2004

	Budgeted Amounts		Actual Amounts	Variance with Final Budget Over/(Under)
	Original	Final		
Beginning budgetary fund balance	<u>\$ 771,900</u>	<u>\$ 779,800</u>	<u>\$ 779,830</u>	<u>\$ 30</u>
Resources (inflows):				
State grants	41,500	42,100	48,923	6,823
Interest	10,000	10,000	11,811	1,811
Other revenue	100	100	-	(100)
Transfers from other funds	<u>158,000</u>	<u>113,300</u>	<u>113,300</u>	<u>-</u>
Amounts available for appropriations	<u>209,600</u>	<u>165,500</u>	<u>174,034</u>	<u>8,534</u>
Charges to appropriations (outflows):				
Public works:				
Construction	264,000	10,000	10,273	273
Routine maintenance	31,000	94,600	91,659	(2,941)
Winter maintenance	30,500	23,700	23,531	(169)
Administration	8,000	8,000	8,000	-
Other	<u>39,500</u>	<u>17,900</u>	<u>12,454</u>	<u>(5,446)</u>
Total charges to appropriations	<u>373,000</u>	<u>154,200</u>	<u>145,917</u>	<u>(8,283)</u>
Ending budgetary fund balance	<u>\$ 608,500</u>	<u>\$ 791,100</u>	<u>\$ 807,947</u>	<u>16,847</u>

OTHER SUPPLEMENTAL INFORMATION

CITY OF HARBOR SPRINGS
Combining Balance Sheet
Nonmajor Governmental Funds
December 31, 2004

<u>Assets</u>	Police Reserve	Historical Commission	Capital Project	Total
Cash	\$ 6,032	\$ 29,657	\$ 93,840	\$ 129,529
Investments	74,028	-	-	74,028
Receivables:				
Accounts	558	267	-	825
Accrued interest	22	108	446	576
Inventory, at cost	-	8,180	-	8,180
Prepaid expenditures	-	245	-	245
 Total assets	 \$ 80,640	 \$ 38,457	 \$ 94,286	 \$ 213,383
 <u>Liabilities and Fund Balances</u>				
Liabilities				
Accounts payable	\$ -	\$ 642	\$ 1,233	\$ 1,875
Accrued expenditures	-	221	-	221
 Total liabilities	 -	 863	 1,233	 2,096
 Fund balances				
Reserved for inventory and prepaids	-	8,425	-	8,425
Unreserved	80,640	29,169	93,053	202,862
 Total fund balances	 80,640	 37,594	 93,053	 211,287
 Total liabilities and fund balances	 \$ 80,640	 \$ 38,457	 \$ 94,286	 \$ 213,383

CITY OF HARBOR SPRINGS
Combining Statement of Revenues, Expenditures, and Changes in Fund Balances
Nonmajor Governmental Funds
For the Year Ended December 31, 2004

	Police Reserve	Historical Commission	Capital Project	Total
Revenues				
Charges for services	\$ -	\$ 1,965	\$ -	\$ 1,965
Interest and investment earnings	8,357	322	2,144	10,823
Other	-	2,260	19,828	22,088
Total revenues	<u>8,357</u>	<u>4,547</u>	<u>21,972</u>	<u>34,876</u>
Expenditures				
Current:				
Public Safety	1,448	-	-	1,448
Recreational and cultural	-	22,171	-	22,171
Capital Outlay	-	-	93,501	93,501
Total expenditures	<u>1,448</u>	<u>22,171</u>	<u>93,501</u>	<u>117,120</u>
Excess (deficiency) of revenues over expenditures	<u>6,909</u>	<u>(17,624)</u>	<u>(71,529)</u>	<u>(82,244)</u>
Other financing sources (uses)				
Operating transfers in	-	27,100	-	27,100
Net change in fund balances	<u>6,909</u>	<u>9,476</u>	<u>(71,529)</u>	<u>(55,144)</u>
Fund balances - beginning of year	<u>73,731</u>	<u>28,118</u>	<u>164,582</u>	<u>266,431</u>
Fund balances - end of year	<u>\$ 80,640</u>	<u>\$ 37,594</u>	<u>\$ 93,053</u>	<u>\$ 211,287</u>

CITY OF HARBOR SPRINGS
Combining Statement of Fiduciary Net Assets
Fiduciary Funds
December 31, 2004

	Agency Funds		Total
	Tax Fund	West Traverse Township Water Fund	
<u>Assets</u>			
Cash	\$ 361,320	\$ 1,887	\$ 363,207
Receivables:			
Taxes	2,582,120	-	2,582,120
Water sales	-	2,593	2,593
Total assets	<u>\$ 2,943,440</u>	<u>\$ 4,480</u>	<u>\$ 2,947,920</u>
<u>Liabilities</u>			
Due to other funds	\$ 39,176	\$ 1,260	\$ 40,436
Due to other governmental units	-	3,220	3,220
Due to County	827,129	-	827,129
Due to School	1,112,458	-	1,112,458
Due to State	51,720	-	51,720
Due to ISD	423,005	-	423,005
Due to College	361,488	-	361,488
Due to Medical Care Facility	75,468	-	75,468
Due to Cemetery	26,336	-	26,336
Due to ambulance and EMS	23,235	-	23,235
Other liabilities	3,425	-	3,425
Total liabilities	<u>\$ 2,943,440</u>	<u>\$ 4,480</u>	<u>\$ 2,947,920</u>